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Qwest.
Spirit of Service™

EX PARTE OR LATE FILED

REDACTED – FOR PUBLIC INSPECTION

Via Courier

EX PARTE

FILED/ACCEPTED
MAY 22 2008
Federal Communications Commission
Office of the Secretary

May 22, 2008

Ms. Marlene H. Dortch, Secretary
Federal Communications Commission
445 12th Street, S.W.
Washington, DC 20554

Re: *In the Matter of Petitions of Qwest Corporation for Forbearance Pursuant to 47 U.S.C. § 160(c) in the Denver, Minneapolis-St. Paul, Phoenix and Seattle Metropolitan Statistical Areas,* WC Docket No. 07-97

Dear Ms. Dortch:

Qwest Corporation hereby submits the attached *ex parte* and request for confidential treatment (pursuant to the First Protective Order) of certain confidential information included in the associated *ex parte*, in the above-captioned proceeding.

One original copy of the non-redacted version is being submitted; and two original copies of the redacted version are being submitted. For both the redacted and non-redacted versions, an extra copy is provided to be stamped and returned to the courier. Both the redacted and non-redacted versions of the *ex parte* are being served on Staff of the Commission's Wireline Competition Bureau as indicated below. This cover letter does not contain any confidential information.

If you have any questions concerning this submission, please contact me using the information reflected in the above letterhead.

Sincerely,

/s/ Melissa E. Newman

No. of Copies rec'd 0+1
List ABCDE

Attachments

cc: (via e-mail)

Denise Coca (denise.coca@fcc.gov)
Jeremy Miller (Jeremy.miller@fcc.gov)
Tim Stelzig (tim.stelzig@fcc.gov)
Gary Remondino (two hard copies of the non-redacted version & via gary.remondino@fcc.gov)

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Daphne E. Butler
Corporate Counsel

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Via Courier

EX PARTE

May 22, 2008

Ms. Marlene H. Dortch, Secretary
Federal Communications Commission
445 12th Street, S.W.
Washington, DC 20554

Re: *In the Matter of Petitions of Qwest Corporation for Forbearance Pursuant to 47 U.S.C. § 160(c) in the Denver, Minneapolis-St. Paul, Phoenix and Seattle Metropolitan Statistical Areas,* WC Docket No. 07-97

Dear Ms. Dortch:

Qwest Corporation ("Qwest") hereby requests confidential treatment of certain information included in the associated attachment. The confidential information includes internal confidential Qwest data as to retail residential and business customers in Omaha.

The confidential information is submitted pursuant to the June 1, 2007 First Protective Order (22 FCC Rcd 10129, DA 07-2292) in WC Docket No. 07-97. As required by the First Protective Order, the confidential information (that is, the non-redacted version) is marked **CONFIDENTIAL – SUBJECT TO FIRST PROTECTIVE ORDER IN WC DOCKET NO. 07-97 BEFORE THE FEDERAL COMMUNICATIONS COMMISSION.** Pursuant to the First Protective Order, Qwest requests that the non-redacted version of the *ex parte* (containing confidential information) be withheld from public inspection.

Qwest considers the confidential information as being competitively-sensitive in nature. This type of information is "not routinely available for public inspection" pursuant to both Federal Communications Commission ("Commission") rules 47 C.F.R. §§ 0.457(d) and 0.459 (as Qwest explained and for which it provided legal justification in its Request for Confidential Treatment and Confidentiality Justification submitted with its four Petitions for Forbearance on April 27, 2007.

Qwest is simultaneously submitting, under separate covers, the non-redacted and redacted versions of this *ex parte*. The redacted version of the *ex parte* is marked **"REDACTED - FOR PUBLIC INSPECTION"**. Both the redacted and non-redacted versions of the *ex parte* are the same except that in the non-confidential version the confidential information in the attachment has been omitted. This letter does not contain any confidential information.

If you have any questions concerning this submission, please call me on 303-383-6653.

Sincerely,

/s/ Daphne E. Butler

Attachment

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Re: *In the Matter of Petitions of Qwest Corporation for Forbearance Pursuant to 47 U.S.C. § 160(c) in the Denver, Minneapolis-St. Paul, Phoenix and Seattle Metropolitan Statistical Areas,* WC Docket No. 07-97

Dear Ms. Dortch:

Qwest Corporation ("Qwest") responds to the white paper by QSI Consulting, Inc. ("QSI"), which Covad, *et al.* filed as an *ex parte* on April 29, 2008. QSI's white paper purports to assess the likely economic impact of granting Qwest's forbearance petitions. In fact, the white paper is flawed. The results are presented in conclusory fashion with extremely few details provided to enable the Federal Communications Commission ("Commission") to determine if there are any errors in QSI's methodology. Moreover, QSI appears to have used very little data, and with the data it did use, rarely shows its work in sufficient detail to allow the Commission to determine if the data were properly utilized.

QSI provides little or no data to back up its assertions that certain economic conditions exist. Moreover, as is shown below, the limited data it *does* provide tend to contradict QSI's theories. For example, QSI asks the Commission to assume that the 1971 article addressing dynamic limit pricing[1] applies to the local competitive telecommunications market that exists today. This theory seeks to describe pricing behavior in a market with one dominant firm and several fringe firms. QSI does not demonstrate that today's local competition market fits this

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[1] *See* Gaskins, Darius W., Jr., "Dynamic Limit Pricing: Optimal Pricing Under Threat of Entry," 3 Journal of Economic Theory 306-22 (1971) and QSI's discussion at pages 24-25.

model. For this model to hold, QSI would have to demonstrate that cable companies and wireless providers, just to name two categories of Qwest's competitors, are fringe providers. QSI has not made such a showing. This is not surprising in light of the rapid growth in the telephony markets that both cable and wireless enjoy. Cable providers continue to win voice customers at a startling rate. Comcast has grown to the number four provider of residential local voice in less than three years.[2] More and more consumers and businesses are shifting voice and data minutes from wireline technologies to wireless technologies. In addition, new forms of competition, such as broadband and Voice over Internet Protocol ("VoIP") providers continue to enter the market to capitalize on growing demand for alternatives to traditional telecommunications services. It is unlikely that QSI can show that rapidly growing competitors, such as cable and wireless, are fringe providers because such a showing would defy reality. Nor has QSI shown that the pricing model applies when there are also competitors in the market that one cannot describe as "fringe."

Similarly, QSI assumes, without proof, that the 1964 article addressing the Theory of Oligopoly is applicable to today's local telecommunications market.[3] Again, QSI does not bother to see if theory really applies to the current facts at issue in this docket. For example, the theory posits a consensus-punishment-detection paradigm. QSI does not, however, present any data at all to show that consensus, punishment and detection exist in today's local telecommunications market.

QSI posits that retail markets are currently constrained by the threat of quick competitive entry based upon Total Element Long Run Incremental cost ("TELRIC")-priced unbundled network elements ("UNEs") but essentially ignores the various other forms of telecommunications competition that currently exist (*e.g.*, cable, fixed and mobile wireless, fiber-based, VoIP, etc.). QSI states that if "the requirement of TELRIC-based pricing for network elements is eliminated, however, the retail markets would not be constrained by the threat of quick competitive entry."[4] However, QSI contradicts itself on page 32 where it lists a number of retail price increases that Qwest has implemented -- at the same time that TELRIC-based UNEs continue to be offered. According to QSI's economic theories, the competitive local exchange carriers ("CLECs") should have quickly entered the residential mass market. Where these residential price increases have occurred, CLECs have not rapidly entered the residential mass market using TELRIC-based UNEs. Instead, the residential market continues to be subject to active competition from cable-based providers, wireless carriers and VoIP providers which all

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[2] *See* http://www.comcast.com/About/PressRelease/PressReleaseDetail.ashx?PRID=721 (visited May 21, 2008).

[3] *See* Stigler, George, "A Theory of Oligopoly," 72 Journal of Political Economy (1964) and QSI's discussion at pages 25-27.

[4] QSI at page 23.

utilize lightly-regulated technologies with different cost structures than UNE-based services. QSI's economic model of the current environment is inaccurate and does not describe actual competitive behavior. QSI's analysis is totally based on speculation founded in economic theories that do not apply to the competitive markets in Phoenix, Denver, Minneapolis-St. Paul, and Seattle. These residential markets are "disciplined" by cable and wireless offerings, resale and QLSP.

In addition to its reliance upon economic models that do not apply to the markets in question, the white paper also betrays QSI's failure to appreciate telecommunications regulation. First, QSI assumes that TELRIC rates replicate competitive market rates.[5] In fact, courts and this Commission have recognized that in reality TELRIC rates do not replicate competitive rates, and that such rates may send misleading signals to the market. For example, in the *UNE Remand Order* this Commission drew a stark contrast between forward-looking rates and market rates. The Commission stated "it would be counterproductive to mandate that the incumbent offers the element at forward-looking prices. Rather, the market price should prevail . . . ."[6] The First Circuit agrees that TELRIC rates are not equivalent to competitive market rates charged for section 271 network elements when section 251 unbundling is no longer required, stating that the "FCC orders provide carriers the authority to charge the potentially higher just and reasonable rates, in order to limit subsidization and to encourage investment by the competitors."[7] Thus, the Commission and the courts recognize that charging TELRIC when section 251 unbundling is no longer required would be "counterproductive" and allowing higher just and reasonable rates will "limit subsidization" and "encourage investment." Qwest has consistently maintained that TELRIC pricing represents a regulatory wholesale pricing mandate designed to "jump start" telecommunications competition by causing Qwest to subsidize its competitors—a mandate that was never intended by Congress in the Telecommunications Act of 1996 to remain in place even after robust competition that does not rely upon section 251 UNEs clearly exists in particular markets.

Second, QSI assumes that because Qwest has not demonstrated inadequate earnings, QSI is justified in not considering any increased profits to Qwest as a benefit, even though corporate profits are generally a positive event.[8] QSI should not draw any conclusions from Qwest's failure to make a showing regarding its earnings. Because Qwest's earnings are not relevant to

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[5] QSI at pages 1, 8.

[6] *In the Matter of Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, Third Report and Order and Fourth Further Notice of Proposed Rulemaking, 15 FCC Rcd 3696, 3906 ¶ 473 (1999) (subsequent history omitted).

[7] *Verizon New Eng., Inc. v. Me. PUC*, 509 F.3d 1, 9 (footnote omitted) (1st Cir.), *reh'g denied*, 509 F.3d 13 (2007).

[8] QSI at page 6 n.13.

the Commission's forbearance analysis, there is no reason for Qwest to make any showing about its earnings. Thus, Qwest's failure to make such a showing demonstrates nothing.

QSI's failure to appreciate federal regulation leads it to misunderstand the likely impact of the petition. For example, QSI mistakenly asserts that granting forbearance from dominant carrier regulation would give Qwest freedom to raise prices for special access loops.[9] In fact, the dominant carrier relief would apply to switched access, not special access. Likewise, QSI states that the grant of forbearance may allow Qwest to increase its federal Subscriber Line Charge to its retail basic exchange residential and business customers.[10] The dominant carrier relief that Qwest seeks would not relieve Qwest from following Title 47, Part 69, which sets out the methodology for calculating the Subscriber Line Charge. Similarly, QSI does not appear to understand that Qwest continues to be bound by "just and reasonable" pricing requirements of section 271 if the Commission grants Qwest's section 251 forbearance request.

QSI calculates the purported impacts for the entire Qwest service footprint in each of the four metropolitan statistical areas ("MSAs"), even though QSI acknowledges that the Commission granted forbearance in only 9 of the 24 wire centers in Qwest's footprint in the Omaha MSA. Qwest has filed for forbearance in all wire centers in each of the four MSAs, and believes such relief is clearly justified by the current market factors. However, if the Commission grants relief only in a subset of the wire centers for which relief is sought (which equaled approximately one third of the 24 wire centers in the Omaha MSA), then QSI's "worst case" estimate – the only estimate it offered – would be drastically overstated.

QSI states that CLECs have few, if any, economically-viable alternatives to UNE DS3 loop and transport services. Qwest can only recover costs of services such as DS3, with rates higher than UNE prices and/or longer term commitments that allow sufficient recovery of the investment to provide the service.

QSI Misunderstands the Wholesale Market

There are numerous flaws in QSI's analysis of the wholesale market. First, QSI does not understand that cable operators do offer loop and transport on a wholesale basis as a direct substitute for similar wholesale services provided by Qwest. QSI states that "cable operators rarely present an economically-viable alternative to Qwest's wholesale loop and transport network elements for a variety of reasons."[11] Contrary to this allegation, Cox's current website shows the availability in Phoenix of its Carrier Access Service, which Cox provides to other carriers and describes as follows:

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[9] QSI at page 13.

[10] *Id.* at page 32.

[11] *Id.* at page 10.

> Cox Carrier Access service is the ideal solution for secure and reliable connections to your voice and data customers. Built on our own fiber-based SONET self-healing network, Cox Carrier Access service gives you high-capacity communications that set the standard for high-speed and high-quality digital transmissions at a cost-effective price.[12]

The Cox Carrier Access options include DS1 loops, DS3 loops and OCn services ranging from OC-3 to OC-192.[13] Further, Cox states that its DS1 and DS3 services "can be fanned out to multiple destinations" on a channelized basis[14] to provide DS0 connections as alternatives to DS0 services offered by Qwest. Obviously, QSI has not checked its facts with McLeodUSA, which stated that Cox offered McLeodUSA wholesale loop and transport services in Omaha and that price is not the reason that McLeodUSA does not obtain wholesale access from the Cox in Omaha.[15]

QSI does not understand Qwest's wholesale offerings. QSI claims that Qwest offered McLeod discounts on special access only if McLeod would forego purchasing UNEs altogether. This is simply not true. As Qwest has previously explained,[16] Qwest offers a number of discount plans, each of which McLeod can take advantage of while continuing to buy UNEs. Customers can pursue discounts on special access by buying out of a tariffed term discount plan (*e.g.*, 36-month term), pursuant to a tariffed Regional Commitment Program ("RCP"), and, where Qwest has pricing flexibility, through contract tariffs. An RCP allows a customer to receive significant price reductions for committing to a minimum quantity of DS1 and/or DS3 circuits (90% of current levels) for a 48-month term. The price reductions are taken from the month-to-month rates. When offered, pricing flexibility contract tariffs are generally added on top of an RCP or term plan in order to provide deeper discounts. In most or all cases these discounts are applied to RCP or term plans that are discounted to begin with.

QSI committed yet another error in its use of Qwest rates in its analysis of wholesale markets. QSI utilized incorrect (55 % higher) Special Access DS1 Loop rates – to which it assumes wholesale rates will be raised – in its analysis of the Denver, Minneapolis, and Seattle MSAs. QSI should have used the Special Access Price Cap rates (FCC No. 1, Section 7).

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[12] http://www.coxbusiness.com/products/other/carrierservices.html (visited May 19, 2008); http://www.coxbusiness.com/systems/index.html (visited May 19, 2008).

[13] http://www.coxbusiness.com/pdfs/cox_carrier.pdf (visited May 19, 2008).

[14] *Id.*

[15] *See* McLeodUSA Telecommunications Services, Inc.'s Reply to Opposition, WC Docket No. 04-223 (filed Sept. 13, 2007) at 3.

[16] *See, e.g.,* Opposition of Qwest Corporation, WC Docket No. 04-223, at 2, *et seq.*

Instead, QSI used the Pricing Flexibility rates (FCC No. 1, Section 17) which are not available in the three MSAs, none of which have been classified by the FCC as areas eligible for Special Access DS1 loop pricing flexibility. QSI also used some incorrect UNE rates, such as the ITP in Minnesota, which actually has a recurring rate of $0, rather than the $0.89 rate that QSI used.[17] In sum, QSI's analysis of the wholesale markets is fraught with errors and should be disregarded in its entirety.

QSI Misunderstands the Retail Market

There are also problems with QSI's analysis of the retail markets. QSI makes undisclosed assumptions for the impacts of four markets it labels: Mass Market Voice; Enterprise Voice; Mass Market Broadband; and Enterprise Broadband. Forty percent of QSI's purported impact is due to the Enterprise Broadband market. QSI seems not to realize that enterprise broadband services, at least as Qwest defines them, utilize network elements that are not offered as unbundled elements. Therefore, any change in the offering of unbundled elements will not impact competition or prices in the "Enterprise Broadband market."

In the retail market, as in the wholesale market, QSI does not understand cable providers' product offerings. QSI states that "cable network[s are] not necessarily constructed to reliably serve most business customers."[18] QSI ignores the large and small business service offerings of both Comcast and Cox that include business class internet, Ethernet dedicated internet, Ethernet network service, Ethernet private line, offsite worker internet services with dedicated support, web hosting, transparent LAN, and virtual private networks. As an example, in the Phoenix MSA, Cox Business has partnered with Shea Commercial Properties, "the largest office condominium developer and brokerage firm in the greater metropolitan Phoenix area,"[19] "to provide tenants with offices that were fully equipped with a variety of voice, video and data services."[20] The Cox-Shea partnership has grown to 4 properties, with more in the planning stages. "In all 4 projects, a vast majority of tenants have chosen Cox Business Services as their provider."[21]

The QSI white paper does not utilize any actual data regarding retail price changes in Omaha or Anchorage that may or may not have occurred following the grant of forbearance to

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[17] QSI at page 14. A recurring rate of zero dollars for a UNE is indicative of the general problem that unbundled network element rates have been set at levels that do not recover the cost of the element; in effect, creating a subsidy by Qwest to its direct competitors.

[18] QSI at page 11 (footnote omitted).

[19] *See* http://www.coxbusiness.com/casestudies/commercial/shea.html (visited May 19, 2008).

[20] *Id.*

[21] *Id.*

test its assumptions for reasonableness. While QSI forecasts a retail price increase post-forbearance, the facts do not bear that out. Qwest's retail customer base in Omaha **[BEGIN CONFIDENTIAL]**

[END CONFIDENTIAL]. Qwest's confidential internal data shows that **[BEGIN CONFIDENTIAL]**

[END CONFIDENTIAL]. CLEC retail customers are apparently switching to Cox (which is now aggressively competing in the residential, small business, Enterprise business and broadband markets) and wireless carriers in Omaha, **[BEGIN CONFIDENTIAL]**

[END CONFIDENTIAL]. On the other hand, Qwest's confidential internal data shows that **[BEGIN CONFIDENTIAL]**

[END CONFIDENTIAL]. In sum, the market *facts* following the forbearance grant in Omaha do not bear out QSI's ill-conceived, poorly documented and mis-applied *theories* about the potential impacts of forbearance in the four MSAs at issue in this docket.

The forbearance process in section 10 exists for the precise purpose of relieving the incumbent local exchange carriers ("ILECs") of the obligation to subsidize their competitors, if and when the Commission finds that facilities-based competition has advanced such that unbundled network elements priced at TELRIC rates are no longer necessary. If Congress had wanted and expected the ILECs to provide below-cost UNEs forever, regardless of the existence of multiple facilities-based competitors, Congress would not have set up the clear process for the ILECs to seek forbearance from section 251 requirements. QSI's deeply flawed analysis will not aid the Commission in determining whether to forbear from section 251 unbundling and it should be afforded no weight.

Respectfully submitted,

/s/ Daphne E. Butler